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C O N F I D E N T I A L SECTION 01 OF 02 MONTERREY 000378

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STATE PASS ONDCP FOR BRAD HITTLE

E.O. 12958: DECL: 10/13/2019
TAGS: PGOV ECON MX
SUBJECT: FORMIDABLE ECONOMIC CHALLENGES FACE NEW NUEVO LEON GOVERNOR

REF: A) MONTERREY 304 B) MONTERREY 292

MONTERREY 00000378 001.2 OF 002

CLASSIFIED BY: Bruce Williamson, Consul General .
REASON: 1.4 (b)

¶1. (U) This is the second in a two part series covering the challenges Nuevo Leon's new administration is facing upon assuming office. This first cable focused on the security and political situation in Nuevo Leon. This cable overviews the fiscal and economic environment in the state government.

¶2. (SBU) Summary: On October 4, Nuevo Leon's newly installed governor, Rodrigo Medina de la Cruz, took over a state government struggling under immediate economic and fiscal burdents. His predecessor, Jose Natividad Gonzalez Paras, left Nuevo Leon as Mexico's most heavily indebted state, hobbled by a dwindling budget and deeply impacted by the world economic downturn. End Summary.

Debt-Straddled

¶3. (U) Immediately, Medina faces a daunting state budget situation. Nuevo Leon is Mexico's most indebted state - total public debt increased over 74 percent during former Governor Jose Natividad Gonzalez Paras' term and now accounts for 51 percent of the state's budget versus a national average of 17 percent. In his last month alone, Gonzalez Paras incurred an additional $250 million in state debt.

¶4. (SBU) Much of this indebtedness went to fund over $3.1 billion in big ticket public works projects such as metro line and highway expansion, construction of Monterrey's "Riverwalk", Nuevo Leon's Command, Control, Communication and Coordination Center (C5), the state's new Innovation and Investigation Park (PIIT), an administrative tower and a pediatric hospital. Medina will be hard pressed to continue spending at this rate. Indeed, a PIIT official recently told EconOff that she was concerned about the park's future viability in the face of uncertain state funding.

Empty Coffers

¶5. (U) In 2009, the state depended on federal revenue sharing to fund most of its $3.1 billion budget, which the central government reduced by $186.9 million in the last half of 2009, forcing the state government to announce $19.5 million in additional emergency spending cuts in July on the heels of an earlier $113 million budget reduction. At the time, state

Secretary of Finance and General Treasury Ruben Martinez Donde, described rural municipalities, which rely wholly on state funding, as "practically broke" (ref A). In 2010, Nuevo Leon is scheduled to receive a further reduction of 10.5 percent in federal funding, making it one of the Mexican states most impacted by federal spending cuts.

Economy Reeling from Recession

¶6. (U) The world economic downturn has hit the state economy, which relies heavily on exports to the U.S., particularly hard. Exports have dropped around 26 percent, foreign direct investment in the state is down around 36 percent (ref F), and recent unemployment figures hover around 7.2 percent - double that of 2003, when the previous administration took office and higher than the national average of 6.2 percent. (Note: Employment figures are derived from Mexican Institute of Social Security (IMSS) and are considered only a rough estimate of the employment situation in Mexico. Mexico has a significant informal economic sector, which does not participate in the IMSS, making aggregate unemployment figures unavailable. End note.)

¶7. (SBU) Yet the state is well positioned to benefit from a U.S. economic rebound and there are signs that the worst may have passed (ref B). A business recovery could give new impetus to the public-private partnerships that the state has created to move forward economic development projects such as the PIIT and other industrial parks.

Comment

¶8. (C) The state's overall economic prospects seem set to brighten somewhat with the advent of a U.S. recovery. However, Nuevo Leon's heavy reliance on shrinking federal subsidies and growing debt service will most likely mean a continuing fiscal crunch. Medina may be frustrated by the prospect of having to

drop or postpone many big-ticket items not yet completed. While the Monterrey metropolitan area is home to around 3.7 million of Nuevo Leon's 4.2 million residents, there are still 500,000 citizens in rural areas that depend on state funding for public services, further constraining Medina's purse. In the end, Gonzalez Paras' spending spree may have left Medina with an impossible legacy and an administration doomed to come up second best in comparison with the previous one.
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